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SUBJECT: Economic Briefing for June 2005

¶1. This cable summarizes selected recent economic events in Taiwan in May 2005:

-- Soft Economy Continues in Q2

-- BenQ Acquires Siemens Cell Phone Unit

-- EVA Air-Boeing Business Ties Remain Strong

-- Taiwan Holds Energy Conference with Mixed Results

-- EZPeer Not Guilty in P2P IPR Case

-- CHT Postpones Privatization Plan

-- Counterfeit Pharmaceutical Seller Nabbed

-- Medical Devices Get Registration Extension

Soft Economy Continues in Q2

¶2. Taiwan's soft economic performance from the first quarter of 2005 spilled over into the second quarter. Weak world demand for Taiwan products has driven y-o-y export growth in May 2005 to its lowest and manufacturing to its most significant contraction since SARS attacked Taiwan in early 2003. Higher petroleum prices and heavy rains together pushed up the inflation rate in May to a new 7-month high. Nevertheless, inflationary pressure is not a concern in light of low money supply growth and declines in price levels for services industries. The unemployment rate in May rose slightly from April, due mainly to new graduates' joining the labor market. Local economists differ in their outlook of economic trends for Taiwan in the next six months. Some suggest the government should stimulate domestic growth rather than relying on export growth.

BenQ Acquires Siemens Cell Phone Unit

¶3. BenQ, one of Taiwan's leading contract manufacturers of electronic consumer goods and a firm that is trying to build its own brand identity, on June 7 announced plans to acquire the cellular phone unit of Siemens, world's fourth largest cell phone brand name. Many analysts have questioned BenQ's decision. Siemens cell phone unit had USD 626 million in losses in 2004. Press reports indicate that BenQ has lost customers for cell phone manufacturing, as other brand name firms take their business elsewhere now that BenQ is a more serious competitor. However, the terms of the deal appear quite favorable to BenQ. BenQ will acquire the Siemens unit without paying any cash. In fact, Siemens will provide BenQ cash and service equal to 250 million euros (about USD 300 million) and purchase 50 million euros (USD 60 million) worth of BenQ's shares as part of the deal. BenQ will acquire the right to use the Siemens brand for 18 months and a BenQ-Siemens brand name for up to five years after the takeover. BenQ Chairman Lee Kun-yao has announced a target of combined operations breakeven in with 2006 sales of US\$10 billion accounting for 11 percent global market share.

EVA Air-Boeing Business Ties Remain Strong

¶4. At a June 27 press conference to unveil GE engines for its new 777-300ER aircraft that will arrive in July 2005, EVA Air President K.W. Chang revealed that the firm is considering replacing its current freighter fleet with Boeing's new 777-200LR cargo plane, which will be available in 2008. EVA is already buying 15 passenger 777s and is looking for eventual replacements for its current cargo

fleet of twelve McDonnell-Douglas MD-11s and four 747-400Fs. In addition, on June 29, EVA Air affiliate Evergreen Aviation Technologies Corporation (EGAT) held a ceremony marking the start of work on the conversion of three 747-400 passenger jets into special cargo freighters that will be used to transport major assemblies used in the production of the Boeing 787 Dreamliner. Modifications to enlarge the upper fuselage of the aircraft will increase the cargo capacity to over that of the 747-400 freighter. Successful completion of the unique aircraft will be a major engineering accomplishment for EGAT. The modified airplane is scheduled to enter service in 2007, and its timely completion will be essential to Boeing and its plans to produce the 787.

Taiwan Holds Energy Conference with Mixed Results

15. Taiwan held its second national energy conference June 20-21. Many energy experts inside and outside the government had hoped that the conference would result in an agreement to rethink Taiwan's anti-nuclear policies in light of the Kyoto Protocol going into effect. Prior to the conference, the appointment of the infamously anti-nuclear Chang Kuo-lung as the head of Taiwan's Environmental Protection Agency was a clear indication that the Chen Administration would remain firm in its anti-nuclear stance. Although the conference agreed to support completion of the construction of the Fourth Nuclear Power Plant, anti-nuclear hardliners prevailed in preventing efforts to extend the lifecycle of existing nuclear power plants and building additional reactors at any of the existing facilities. In addition, the conference made many claims about how Taiwan will reduce its carbon emissions. Environmental groups view the claims as empty rhetoric in light of the fact that the conference did not decide to hinder the approval of controversial projects including a steel plant, a naptha cracker plant and three new coal-fired plants. Combined these five projects will increase Taiwan's CO2 emissions by 20 percent.

EZPeer Not Guilty in P2P IPR Case

16. Taipei's Shilin District Court on June 30 announced its decision on the criminal copyright infringement case based on a complaint brought by the International Federation of Phonographic Industries (IFPI) against peer-to-peer (P2P) software provider EZPeer. The Court ruled that providing P2P service is not illegal under Taiwan law, that EZPeer did not illegally reproduce or transmit copyrighted materials, and that EZPeer is not guilty of copyright infringement. The Taiwan branch of IFPI vowed to appeal the decision. The Court's decision did not address the matter of civil liability and stated clearly that EZPeer members who use P2P services to transmit copyrighted materials may be prosecuted for criminal copyright infringement. The decision is a blow to efforts to protect copyrights in Taiwan and illustrates the difficulties rightsholders face when using Taiwan's judicial process to protect their intellectual property (IP).

CHT Postpones Privatization Plan

17. Chairman HO-CHEN Tan told a Chunghwa Telecom (CHT) shareholders meeting on June 21 that continued concerns over employee benefits would delay until August the planned privatization of CHT through the sale of 17 percent of CHT shares. However Ho-chen insisted that CHT remains committed to privatization, in spite of the Legislative Yuan's passage of a resolution calling on the government to suspend the share sale. After Ho-chen's statement, CHT union leaders postponed a planned July 1 strike, but are still preparing to travel to the U.S. to protest during Chairman Ho-chen's upcoming roadshow. Industry insiders agree that the sale will go forward despite the union's protests.

Counterfeit Pharmaceutical Seller Nabbed

18. Prompted by an investigative news report that some of the popular weight-loss drug Reductil (manufactured by Abbott Laboratories) sold over the internet was counterfeit, special agents of the Criminal Investigation Bureau raided a residence in Taipei County on May 24 and arrested one suspect. The suspect told police that she had both purchased and sold the products online and was unaware that they were counterfeit. Abbott's Taiwan manager estimated that as much as 20 percent of Reductil sales in Taiwan could be counterfeits.

Medical Devices Get Registration Extension

19. Unable to meet its own June 20 deadline for registering medical devices, the Taiwan Department of Health (DOH)

issued an administrative notice allowing manufacturers and importers to continue to import medical devices for an additional six months. Medical device manufacturers that have applied for registration of their products but have not yet received licenses will be allowed to continue to import their products until December 20, 2005. Those manufacturers that did not apply for registration by June 20, 2005 will not benefit from this amendment. Those products that have been registered and have received import licenses (as of June 17 barely 200 out of more than 4000 applications) can be imported without restriction.

KEEGAN